

Interest on Deposits — Part 329

Introduction

The procedures and guidance in this section apply to demand deposits and negotiable orders of withdrawal (NOW) accounts held at banks. Banks are prohibited from paying interest on demand deposits. However, NOW accounts are not considered “demand deposits” when the entire beneficial interest of the deposit is held by certain eligible depositors.

Regulation Overview

Part 329 of the FDIC regulations prohibits the payment of interest by banks on any demand deposit.

A demand deposit includes any deposit payable on demand; or any deposit with an original maturity or required notice period of less than seven days; or any deposit representing funds for which the bank does not reserve the right to require at least seven days’ written notice of intended withdrawal; or any other deposit which the depositor is authorized to make more than six preauthorized or automatic transfers or makes more than three of these transfers by check, draft, debit card or similar order.

NOW accounts are interest bearing accounts from which depositors are permitted to make withdrawals by negotiable or transferable instruments for funds transfers to third parties. NOW accounts can be maintained by the following entities, and would not be considered demand deposits under the regulation:

- One or more individuals, including sole-proprietorships.
- A not-for-profit organization operated primarily for religious, philanthropic, charitable, educational, political, or other similar purpose.
- Officers, employees, or agents of public entities (public funds).
- Funds held in a fiduciary capacity (bank trust department, individual fiduciary, or trustee in bankruptcy), provided that all beneficiaries are natural persons.

The regulation also provides guidance on allowable transfers for nondemand deposits, interest and premiums, and interest and ten-day grace period for time and savings deposits.

Definitions

“Cash Management Arrangements” Cash management services provided by financial institutions sometimes include offering sweep accounts and repurchase agreements. Regulatory compliance for these activities is generally reviewed during risk management examinations and during nondeposit product reviews. However, examiners should be aware that Section 329.2 concerning the prohibition of paying

interest on demand deposits could be violated based on the definitions of Money Market Deposit Accounts (MMDA) and savings accounts for excessive transactions.

“Money Market Deposit Account (MMDA)” An MMDA is a savings deposit that permits, under the terms of the deposit contract or by practice of the financial institution, the depositor to make no more than six transfers and withdrawals per calendar month or statement cycle of at least four weeks to another account of the depositor or to a third party.

No more than three of the six transfers can be made by check, draft, debit card, or similar order to a third party. The following transfers are not included in the six transfer limitation:

- Transfers to the financial institution for the purpose of repaying loans and associated expenses (as originator or servicer).

NOTE: This exemption “does not apply to transfers to the financial institution that are made for the purpose of repaying loans that are made by the financial institution to the depositor’s demand deposit account for the purposes of covering overdrafts.” (§329.1(b)(3))

- Transfers to another account of the depositor made by mail, messenger, automated teller machine (ATM), or in person.
- Withdrawals made by mail, messenger, telephone (via check mailed to the depositor), ATM, or in person.

Refer to §204.2(d) of Regulation D and the Interpretative Rule found in Section 329.101 for more guidance on MMDAs.

NOTE: Personal computer (PC) transfers should be treated just like telephone transactions and would be included in the “six” transfers and withdrawals if the PC transfer was preauthorized or automatic.

“NOW Account” NOW Accounts are deposit accounts which consist solely of funds in which the entire beneficial interest is held by:

- One or more individuals, including sole-proprietorships.
- A not-for-profit organization operated primarily for religious, philanthropic, charitable, educational, political, or other similar purpose.
- Officers, employees, or agents of public entities (public funds).
- Funds held in a fiduciary capacity (bank trust department, individual fiduciary, or trustee in bankruptcy), provided that all beneficiaries are natural persons.

The following types of entities **are not** eligible to maintain NOW accounts:

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- Corporations
- For-profit partnerships, including a husband and wife partnership
- Individuals who have incorporated, such as Professional Associations (PA)
- Trust accounts where the beneficial interest is held by two or more unrelated parties, such as realty trusts

Refer to the following regulatory provisions for guidance on the definition of a NOW account:

- 12 USC 1832(a), NOW accounts (This citation is the Act which created NOW accounts.)
- Section 329.1(b)(3), footnote 1 (This footnote quotes 12 USC 1832(a) in its entirety.)
- Regulation D, Section 204.2
- Regulation D, Section 204.130 (This is an interpretative section providing further guidance on the eligibility of certain entities to maintain NOW accounts.)

“Savings Accounts” Accounts that are subject to the same transaction limitations as MMDAs (including passbook savings accounts and statement savings accounts).

Examination Objectives

The examination objectives are to:

- Determine whether a bank is effectively managing the compliance risks associated with demand deposit accounts and NOW accounts.
- Assess compliance with the applicable law and regulation.
- Implement corrective actions to address compliance deficiencies and ensure future compliance.

Examination Procedures

Evaluate for Compliance with Part 329

1. Determine which of the following accounts the financial institution offers:
 - Demand deposits (non-interest bearing checking accounts)
 - Savings accounts
 - Negotiable Order of Withdrawal (NOW) accounts
 - Money Market Deposit Accounts (MMDA)
 - Time deposits
2. Interview personnel responsible for opening NOW accounts to ensure they know the requirements and prohibitions of Section 329.1.
3. Determine the category of account according to the activity allowed for that particular account.

*NOTE: Even though an account may be classified by the financial institution as one of the above, **the activity allowed within the account** dictates the actual definition. For example, an account which exceeds the monthly transfer or check processing limits should no longer be classified as a savings account but as a DDA or NOW Account by the institution. Refer to Section 204.2 of Regulation D for account definitions.*

NOW Accounts

4. Determine whether the entire beneficial ownership interest of a NOW account is held by one of the following eligible individuals or entities:
 - One or more individuals, including sole proprietorships
 - A not-for-profit organization operated primarily for religious, philanthropic, charitable, educational, political, or other similar purposes
 - A government unit of the United States, or any state, county, or municipality of the United States, or any United States territory or possession
 - A fiduciary (either individual or corporate) if the beneficiary is otherwise eligible to maintain a NOW account
 - Pension funds, escrow accounts, and security deposits if the entire beneficial interest is held by one of the eligible individuals or entities listed above.

If an account holder(s) does not meet the above definitions, it is ineligible to maintain a NOW account. For example, for-profit partnerships and corporations are ineligible.

Refer to Section 204.130 of Regulation D for further guidance.

5. Determine if the financial institution has adequate internal controls to ensure that ineligible entities do not maintain NOW accounts.
 - Review the NOW account trial balance:

Use existing records, but if warranted, request a full name listing of the trial balance as opposed to a short name version. A short name listing may not include certain portions of the account title; therefore, some ineligible accounts could be missed during the review.
 - Select questionable accounts, including but not limited to the examples below, for documentation review:
 - Accounts which include the designations “Inc.,” “Corp.,” “LLC” (Limited Liability Corporation) or “P.C.” (Professional Corporation), which imply an incorporated entity.
 - Accounts which include the designation “partnership,” “limited partnership,” or “general partnership”.